

RUSSELL COUNTY SCHOOL DISTRICT
BASIC FINANCIAL STATEMENTS,
SUPPLEMENTARY INFORMATION,
AND INDEPENDENT AUDITOR'S REPORTS

Year Ended June 30, 2005

RUSSELL COUNTY SCHOOL DISTRICT

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INDEPENDENT AUDITOR'S REPORT

Members of the Board of Education
Russell County School District
Jamestown, Kentucky

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Russell County School District as of and for the year ended June 30, 2005, which collectively comprise the District's basic financial statements, as listed in the accompanying table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirements prescribed by the Kentucky State Committee for School District Audits in Appendix I of the Independent Auditor's Contract - General Audit Requirements, Appendix II of the Independent Auditor's Contract - State Audit Requirements, and Appendix III of the Independent Auditor's Contract - Electronic Submission. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the District as of June 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued a report dated September 23, 2005, on our consideration of Russell County School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Management's Discussion and Analysis on pages 3 through 9, and the Budgetary Comparison Information on pages 36 through 37 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Russell County School District's basic financial statements. The combining financial statements as listed in the accompanying table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Also, the accompanying Schedule of Expenditures of Federal Awards on pages 42 through 43 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Stiles, Carter & Associates

Certified Public Accountants
September 23, 2005

REQUIRED SUPPLEMENTARY INFORMATION

RUSSELL COUNTY SCHOOL DISTRICT – JAMESTOWN, KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2005

The discussion and analysis of Russell County School District's financial performance provides an overall review of the School District's financial activities for the fiscal year ended June 30, 2005. The intent of this discussion and analysis is to review the School District's financial performance as a whole; readers should also review the financial statements and notes to the financial statements to enhance their understanding of the School District's financial performance.

The Management's Discussion and Analysis (MD&A) is an element of the new reporting model adopted by the Governmental Accounting Standards Board (GASB) in the Statement No. 34 *Basic Financial Statements and Management's Discussion and Analysis for State and Local governments* issued in June 1999.

FINANCIAL HIGHLIGHTS

- The beginning cash balance for the District was \$6.4 million. The ending cash balance was \$8.9 million. This ending balance includes \$6.3 million in construction funds.
- Following the completion of the District long-range plan for facilities, there is a focus on renovation of facilities and additional educational space.
- The Board completed the new Jamestown Elementary School. The Board also began the renovation projects at Salem and Union Chapel Elementary Schools and issued bonds for the project.
- The General Fund had \$18.3 million in revenue, which primarily consisted of the state program (SEEK), property, utilities, and motor vehicle taxes. Excluding inter-fund transfers, there were \$19.5 million in General Fund expenditures.
- Bonds are issued as the District renovates facilities consistent with a long-range facilities plan that is established with community input and in keeping with Kentucky Department of Education (KDE) stringent compliance regulations. The District's total debt increased by \$6,065,000 during the current fiscal year.

USING THIS ANNUAL REPORT

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of activities presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The government-wide financial statements outline functions of the District that are principally supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the District include instruction, support services, operation and maintenance of plant, student transportation and operation of non-instructional services. Fixed assets and related debt is also supported by taxes and intergovernmental revenues.

The government-wide financial statements can be found on pages 10 - 11 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. This is a state mandated uniform system and chart of accounts for all Kentucky public school districts utilizing the MUNIS administrative software. The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into three categories: governmental, proprietary funds and fiduciary funds. The only fiduciary funds are agency funds for student education. The only proprietary funds are our food service and childcare operations. All other activities of the District are included in the governmental funds.

The basic governmental fund financial statements can be found on pages 12 - 19 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 20 - 35 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$10.6 million as of June 30, 2005.

The largest portion of the District's net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, furniture and equipment and construction in progress), less any related debt used to acquire those assets that is outstanding. The District uses these capital assets to provide services to its students; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

(Table 1)
Net Assets

	Governmental Activities		Business-type Activities		Total Primary Government	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Current and Other Assets	\$ 9,436,798	\$ 6,744,198	\$ 89,536	\$ 89,536	\$ 9,526,334	\$ 6,833,734
Capital Assets	<u>25,478,774</u>	<u>23,180,763</u>	<u>987,302</u>	<u>987,302</u>	<u>26,466,076</u>	<u>24,168,065</u>
Total Assets	<u>34,915,572</u>	<u>29,924,961</u>	<u>1,076,838</u>	<u>1,076,838</u>	<u>35,992,410</u>	<u>31,001,799</u>
Long-term Debt	23,513,190	17,585,675	-	-	23,513,190	17,585,675
Other Liabilities	<u>1,852,433</u>	<u>1,992,619</u>	<u>-</u>	<u>-</u>	<u>1,852,433</u>	<u>1,992,619</u>
Total Liabilities	<u>25,365,623</u>	<u>19,578,294</u>	<u>-</u>	<u>-</u>	<u>25,365,623</u>	<u>19,578,294</u>
Net Assets						
Investment in capital assets (net of debt)	1,773,955	4,741,620	987,302	987,302	2,761,257	5,728,922
Restricted	6,444,531	2,233,901	-	-	6,444,531	2,233,901
Unrestricted	<u>1,331,463</u>	<u>3,371,146</u>	<u>89,536</u>	<u>89,536</u>	<u>1,420,999</u>	<u>3,460,682</u>
Total Net Assets	<u>\$ 9,549,949</u>	<u>\$ 10,346,667</u>	<u>\$ 1,076,838</u>	<u>\$ 1,076,838</u>	<u>\$ 10,626,787</u>	<u>\$ 11,423,505</u>

The following are significant current year transactions that have had an impact on the Statement of Net Assets.

The District issued \$6,720,000, in revenue bonds and incurred significant expenditures related to the construction of Jamestown Elementary School and the renovation of Salem and Union Chapel Elementary Schools. The District also incurred additional personnel costs.

Comments on Budget Comparisons

- The District's total revenues for the fiscal year ended June 30, 2005, net of Interfund transfers, were \$24.7 million.
- General fund budget compared to actual revenue varied slightly from line item to line item with the ending actual balance being \$4.9 million more than budget or approximately 37%. This includes on-behalf payments of \$3.5 million.
- The total cost of all programs and services was \$26.1 million including debt service.
- General fund budget expenditures to actual varied significantly in Instruction, District Administrative Support, School Administrative Support, and Plant. Instruction expenditures were more than budget because the District did not budget on-behalf payments in accordance with Kentucky Department of Education requirements. School Administrative was more due to personnel costs. District Administrative and Plant expenditures were less than budget because of the District's contingency budget and not having to spend funds for plant capital additions.

The following Table 2 presents a summary of changes in net assets for the fiscal years ended June 30, 2005 and 2004.

(Table 2)
Changes in Net Assets

	Governmental Activities		Business-type Activities		Total Primary Government	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
REVENUES:						
Program revenues:						
Charges for services	\$ 62,767	\$ 181,464	\$ 431,749	\$ 390,211	\$ 494,516	\$ 571,675
Operating grants and contributions	4,415,059	4,419,564	899,298	919,445	5,314,357	5,339,009
Capital grants and contributions	446,243	430,339	-	-	446,243	430,339
General revenues:						
Property taxes	2,591,964	2,382,623	-	-	2,591,964	2,382,623
Motor vehicle taxes	500,645	501,503	-	-	500,645	501,503
Utility taxes	808,473	706,220	-	-	808,473	706,220
Other taxes	10,018	8,960	-	-	10,018	8,960
Investment earnings	215,171	287,056	707	781	215,878	287,837
State and formula grants	14,093,915	12,888,952	-	-	14,093,915	12,888,952
Miscellaneous	193,163	-	-	-	193,163	-
Gain (loss) on asset disposal	4,718	16,358	(16,854)	(363)	(12,136)	15,995
Total revenues	<u>23,342,136</u>	<u>21,823,039</u>	<u>1,314,900</u>	<u>1,310,074</u>	<u>24,657,036</u>	<u>23,133,113</u>
EXPENSES						
Program Activities						
Instruction	14,330,187	13,069,847	-	-	14,330,187	13,069,847
Student support	1,349,202	1,275,546	-	-	1,349,202	1,275,546
Instructional staff support	1,461,634	1,138,431	-	-	1,461,634	1,138,431
District administrative support	677,545	503,019	-	-	677,545	503,019
School administrative support	1,135,415	1,012,255	-	-	1,135,415	1,012,255
Business support	618,102	227,803	-	-	618,102	227,803
Plant operation and maintenance	1,778,278	1,551,043	-	-	1,778,278	1,551,043
Student transportation	1,501,645	1,317,923	-	-	1,501,645	1,317,923
Central office support	-	188,739	-	-	-	188,739
Facilities acquisition	65,526	-	-	-	65,526	-
Community service activities	351,568	424,224	-	-	351,568	424,224
Interest costs	725,190	794,093	-	-	725,190	794,093
Business-type Activities:						
Food service	-	-	1,385,184	1,324,036	1,385,184	1,324,036
FRC Childcare	-	-	76,273	73,872	76,273	73,872
Total expenses	<u>23,994,292</u>	<u>21,502,923</u>	<u>1,461,457</u>	<u>1,397,908</u>	<u>25,455,749</u>	<u>22,900,831</u>
Transfers	(144,554)	-	144,554	-	-	-
Increase (decrease) in net assets	<u>\$ (796,710)</u>	<u>\$ 320,116</u>	<u>\$ (2,003)</u>	<u>\$ (87,834)</u>	<u>\$ (798,713)</u>	<u>\$ 232,282</u>

Governmental Activities

Instruction comprises 60% of governmental program expenses. Support services expenses make up 35% of government expenses. The remaining expense for interest, uncapitalized facilities acquisition and community service activities or the remaining 5% of total government expense.

The Statement of Activities shows the cost of program services and the charges for services and grants offsetting those services. Table 3 shows, for government activities, the total cost of services and the net cost of services. That is, it identifies the cost of these services supported by tax revenue and unrestricted State entitlements.

(Table 3)
Governmental Activities Total
Cost of Services

	Cost of Services		Net Cost of Services	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Instruction	\$ 14,330,187	\$ 12,645,623	\$ 10,799,658	\$ 9,699,215
Support services	8,493,018	7,679,083	7,877,572	6,332,118
Facilities acquisition	65,526	-	65,526	-
Community services	351,568	424,224	3,813	76,469
Interest costs	753,993	753,993	323,654	323,654
Total expenses	<u><u>\$ 23,994,292</u></u>	<u><u>\$ 21,502,923</u></u>	<u><u>\$ 19,070,223</u></u>	<u><u>\$ 16,431,456</u></u>

Business-Type Activities

The business-type activities are the food service operation and childcare operation. These programs had total revenues of \$1,314,900 and expenses of \$1,461,457 for fiscal year 2005. Of the revenues, \$431,749 was charges for services, \$899,298 was from State and Federal grants and \$781 was from investment earnings. Loss on disposal of assets was \$16,854 due to the removal of the portion of the old Jamestown Elementary School included in fixed assets. The food service fund also received a transfer from the construction fund for \$144,554 to purchase equipment at the new Jamestown Elementary School. Business activities receive no support from tax revenues. The School District will continue to monitor the charges and costs of this activity. If it becomes necessary, the School District will increase the charges for this activity.

The School District's Funds

Information about the School District's major funds starts on page 12. These funds are accounted for using the modified accrual basis of accounting. All governmental funds had total revenues and other financing sources of \$31,655,607 and expenditures and other financing uses of \$28,669,726. Net changes in fund balances for the year were most significant in General Fund (\$1,024,317) and Construction Fund \$3,935,750.

The decrease in General Fund was due to funds used for capital outlay and additional personnel costs. The Construction Fund increase was due to unspent bond proceeds on the Salem and Union Chapel Elementary School renovation projects and the spending of prior year bond funds on the Jamestown Elementary School project.

General Fund-Budget Highlights

The School District's budget is prepared according to Kentucky law and is based on accounting for certain transactions on a basis of cash receipts, disbursements and encumbrances. The most significant budgeted fund is the General Fund. The State Department of Education requires a zero-based budget with any budgeted remaining fund balance shown as a contingency expense in the budget process.

For the General Fund revenues were budgeted at \$13,414,000 with actual amounts of \$18,298,486. Budgeted expenditures of \$16,755,716 compare with actual expenditures of \$19,453,947. The most significant fluctuation is for on-behalf payments of \$3,524,575. If on-behalf payments were not included in revenues, revenues would be \$14,773,911, which is \$1,359,911 over budget. If on-behalf payments were not included in expenditures, expenditures would be \$15,929,372, which is \$826,344 under budget.

Capital Assets and Debt Administration

Capital Assets

At the end of fiscal year 2005 the School District had \$26,548,335 invested in land, buildings, equipment, construction in progress, and \$25,478,774 in governmental activities. Table 4 shows fiscal year 2005 and 2004 balances.

(Table 4)
Capital Assets
(Net of Depreciation)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2005	2004	2005	2004	2005	2004
Land and land improvements	\$ 1,191,458	\$ 1,259,410	\$ -	\$ -	\$ 1,191,458	\$ 1,259,410
Buildings and improvements	21,863,867	16,120,277	824,557	862,289	22,688,424	16,982,566
Technology	321,868	250,860	-	-	321,868	250,860
Vehicles	1,175,857	983,025	-	-	1,175,857	983,025
General equipment	287,666	299,868	245,004	125,013	532,670	424,881
Total	24,840,716	18,913,440	1,069,561	987,302	25,910,277	19,900,742
Construction in progress	638,058	4,267,323	-	-	638,058	4,267,323
Total	<u>\$ 25,478,774</u>	<u>\$ 23,180,763</u>	<u>\$ 1,069,561</u>	<u>\$ 987,302</u>	<u>\$ 26,548,335</u>	<u>\$ 24,168,065</u>

Table 5 shows changes in capital assets for the years ended June 30, 2005 and 2004.

(Table 5)
Change in Capital Assets

	Governmental Activities		Business-type Activities		Total Primary Government	
	2005	2004	2005	2004	2005	2004
Beginning balance	\$ 23,180,763	\$ 19,152,731	\$ 987,302	\$ 1,026,821	\$ 24,168,065	\$ 20,179,552
Additions	9,633,747	4,905,310	153,474	4,647	9,787,221	4,909,957
Retirements	(6,327,571)	(296,241)	(16,854)	(5,908)	(6,344,425)	(302,149)
Depreciation	(1,008,165)	(581,037)	(54,361)	(38,258)	(1,062,526)	(619,295)
Ending balance	<u>\$ 25,478,774</u>	<u>\$ 23,180,763</u>	<u>\$ 1,069,561</u>	<u>\$ 987,302</u>	<u>\$ 26,548,335</u>	<u>\$ 24,168,065</u>

Construction was completed a new Jamestown Elementary School. A project started on the renovation of Salem and Union Chapel Elementary Schools. This unfinished project cost is in construction in progress at June 30, 2005.

Debt

At June 30, 2005 and 2004, the School District had \$21,615,000 in bonds outstanding, of this amount \$2,347,922 is to be paid from the KSFCC funding provided by the State of Kentucky. A total of \$890,000 is due within one year of June 30, 2005. The District issued bonds for \$6,720,000 during the fiscal year for the Salem and Union Chapel renovation projects.

District Challenges for the Future

Russell County School District's financial status has declined in the last fiscal year. This was a result of additional personnel costs including standard raises and additional staffing requirements for special education. Also, the General Fund made financial contributions to the Jamestown Elementary School project. In addition, the District is required to assume additional costs due to continued student growth without increased state funding due to the growth and various unfunded mandates. Because of these issues, long-term financial strategies will need to be implemented through the budgeting process.

The School District has experienced an annual growth in student enrollment of 25-58 students per year, for the last 3 years. The School District has prepared for an increase in enrollment by building new schools and renovating and adding to existing schools. These new facilities come with increased utility costs and additional personnel cost (both administrative and support staffs). These new buildings also have a cost for computers, library books, instructional materials, and other items that are primarily paid from the General Fund. In addition, the District continues to face rising fuel and natural gas costs. These costs along with the need to maintain facilities in the next few years will create more challenges for the School District.

The costs associated with growth have in the past been offset due to increased student enrollment producing additional state funding, and continued increases in business and residential property subject to tax within the School District. Our property tax base continues to grow; however our School District, like all Kentucky School Districts, is limited to a 4% annual growth in property tax revenue on existing property.

Additional factors concerning our School District's financial status include the implementation of various unfunded mandates. Examples include the Flex Fund accounts (Professional Development, Safe Schools, Preschool, Textbooks and Extended School Services). State funding for these programs does not meet our needs as a District. Therefore, local generated funds will have to address these areas. Also, the uncertainty of state budgeted revenue projections may impact our funding as well as future mandated salary increases for all certified personnel. In addition, the full effect of No Child Left Behind (NCLB) has yet to be determined. Funding for this program is not equal to the mandates required by the Federal Government.

With careful planning and monitoring of our finances, Russell County Schools' goal is to continue to provide a quality education for our students and a secure financial future for the School District.

Contacting the School District's Financial Management

This financial report is designed to provide our citizens, taxpayers, and investors and creditors with a general overview of the School District's finances and to show the School District's accountability for the money it receives. If you have any question about this report or need additional information, contact John Loy, 404 S. Main St., P.O. Box 440, Jamestown, Kentucky 42629.

BASIC FINANCIAL STATEMENTS

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF NET ASSETS

June 30, 2005

Assets	Governmental Activities	Business- Type Activities	Total
<u>Current Assets</u>			
Cash and cash equivalents	\$ 8,870,491	\$ -	\$ 8,870,491
Inventory		21,163	21,163
Due from other funds	10,086	52	10,138
Accounts receivable:			
Taxes-current	106,406		106,406
Accounts receivable	129,113		129,113
Intergovernmental-State	50,546		50,546
Intergovernmental-Indirect Federal	255,847		255,847
Intergovernmental-Direct Federal	7,974		7,974
Interest receivable	6,335		6,335
Total Current Assets	9,436,798	21,215	9,458,013
<u>Noncurrent Assets</u>			
Capital assets	36,629,416	1,531,375	38,160,791
Less: accumulated depreciation	(11,150,642)	(461,814)	(11,612,456)
Total Noncurrent Assets	25,478,774	1,069,561	26,548,335
Total Assets	34,915,572	1,090,776	36,006,348
Liabilities			
<u>Current Liabilities</u>			
Accounts payable	416,130	2,646	418,776
Cash overdraft		3,209	3,209
Due to other funds	52	10,086	10,138
Accrued liabilities	429		429
Deferred revenue	58,129		58,129
Current portion of bond obligations	890,000		890,000
Current portion of capital lease obligations	178,461		178,461
Current portion of accrued sick leave	103,969		103,969
Interest payable	205,263		205,263
Total Current Liabilities	1,852,433	15,941	1,868,374
<u>Noncurrent Liabilities</u>			
Noncurrent portion of bond obligations	20,725,000		20,725,000
Less: Bond discount and expense	(250,322)		(250,322)
Noncurrent portion of capital lease obligations	2,161,680		2,161,680
Noncurrent portion of accrued sick leave	876,832		876,832
Total Noncurrent Liabilities	23,513,190	-	23,513,190
Total Liabilities	25,365,623	15,941	25,381,564
<u>Net Assets</u>			
Invested in capital assets, net of related debt	1,773,955	1,069,561	2,843,516
Restricted for:			
Capital projects	6,429,577		6,429,577
Debt service	14,954		14,954
Unrestricted	1,331,606	5,274	1,336,880
Total Net Assets	\$ 9,550,092	\$ 1,074,835	\$ 10,624,927

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT
STATEMENT OF ACTIVITIES
Year Ended June 30, 2005

FUNCTIONS/PROGRAMS

Governmental Activities:

Instruction	\$ 14,330,187	\$ 62,767	\$ 3,467,762	\$ -	\$ (10,799,658)	\$ -	\$ (10,799,658)
Support services:							
Student	1,349,202		76,429		(1,272,773)		(1,272,773)
Instruction staff	1,461,634		494,316		(967,318)		(967,318)
District administrative	677,545				(677,545)		(677,545)
School administrative	1,135,415				(1,135,415)		(1,135,415)
Business	618,102		13,143		(604,959)		(604,959)
Plant operation and maintenance	1,778,278				(1,778,278)		(1,778,278)
Student transportation	1,501,645		15,654		(1,485,991)		(1,485,991)
Facility acquisition	65,526				(65,526)		(65,526)
Community service activities	351,568		347,755		(3,813)		(3,813)
Interest on long-term debt	725,190			446,243	(278,947)		(278,947)

Total Governmental Activities

	23,994,292	62,767	4,415,059	446,243	(19,070,223)	-	(19,070,223)
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Business-Type Activities:

Food service	1,385,184	367,380	887,756			(130,048)	(130,048)
Childcare	76,273	64,369	11,542			(362)	(362)

Total Business-Type Activities

	1,461,457	431,749	899,298	-	-	(130,410)	(130,410)
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Total Primary Government

	\$ 25,455,749	\$ 494,516	\$ 5,314,357	\$ 446,243	(19,070,223)	(130,410)	(19,200,633)
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General Revenues:

Taxes:

Property taxes	2,591,964				2,591,964		2,591,964
Motor vehicle taxes	500,645				500,645		500,645
Utility taxes	808,473				808,473		808,473
Other	10,018				10,018		10,018
Investment earnings	215,171					707	215,878
State and formula grants	14,093,915				14,093,915		14,093,915
Transfers	(144,554)					144,554	-
Miscellaneous	193,163				193,163		193,163
Gain (loss) on disposal of fixed assets	4,718				(16,854)		(12,136)

Total general revenues

	18,273,513				18,273,513	128,407	18,401,920
--	------------	--	--	--	------------	---------	------------

Change in net assets

	(796,710)				(796,710)	(2,003)	(798,713)
--	-----------	--	--	--	-----------	---------	-----------

Net assets - beginning

	10,346,659				10,346,659	1,076,838	11,423,497
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Net assets - ending

	\$ 9,549,949				\$ 9,549,949	\$ 1,074,835	\$ 10,624,784
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FUND FINANCIAL STATEMENTS

RUSSELL COUNTY SCHOOL DISTRICT

BALANCE SHEET

GOVERNMENTAL FUNDS

June 30, 2005

	General Fund	Special Revenue	Construction Fund	Other Governmental Funds	Total Governmental Funds
Assets and Resources:					
Cash and cash equivalents	\$ 2,185,107	\$ -	\$ 6,319,255	\$ 434,409	\$ 8,938,771
Accounts receivable:					
Taxes - current	106,406				106,406
Accounts receivable	122,493	6,620			129,113
Intergovernmental - State		50,546			50,546
Intergovernmental - Indirect Federal		255,847			255,847
Intergovernmental - Direct Federal		7,974			7,974
Due from other funds	10,086	5,547			15,633
Interest receivable	6,335				6,335
Total Assets and Resources	<u>\$ 2,430,427</u>	<u>\$ 326,534</u>	<u>\$ 6,319,255</u>	<u>\$ 434,409</u>	<u>\$ 9,510,625</u>
Liabilities and Fund Balances:					
Liabilities					
Cash overdraft	\$ -	\$ 68,275	\$ -	\$ -	\$ 68,275
Accrued liabilities	429				429
Accounts payable	106,997		309,133		416,130
Deferred revenue		58,129			58,129
Due to other funds	5,599				5,599
Total Liabilities	113,025	126,404	309,133	-	548,562
Fund Balances					
Reserved for:					
Construction			6,010,122		6,010,122
Encumbrances	75,289				75,289
SFCC escrow				419,455	419,455
Debt service				14,954	14,954
Unreserved:					
Undesignated, reported in:					
General fund	2,242,113				2,242,113
Special revenue funds		200,130			200,130
Total Fund Balances	<u>2,317,402</u>	<u>200,130</u>	<u>6,010,122</u>	<u>434,409</u>	<u>8,962,063</u>
Total Liabilities and Fund Balances	<u>\$ 2,430,427</u>	<u>\$ 326,534</u>	<u>\$ 6,319,255</u>	<u>\$ 434,409</u>	<u>\$ 9,510,625</u>

RUSSELL COUNTY SCHOOL DISTRICT

RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS TO
THE STATEMENT OF NET ASSETS

June 30, 2005

Total fund balance per fund financial statements	\$ 8,962,063
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Amounts reported for governmental activities in the statement of net
assets are different because:

Capital assets are not reported in this fund financial statement because they are not current financial resources, but they are reported in the statement of net assets.	25,478,774
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Certain liabilities (such as bonds and capital leases, certain payables, accrued sick leave, and accrued interest) are not reported in this fund financial statement because they are not due and payable, but they are presented in the statement of net assets.	<u>(24,890,888)</u>
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Net assets for governmental activities	<u>\$ 9,549,949</u>
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RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

GOVERNMENTAL FUNDS

Year Ended June 30, 2005

	General Fund	Special Revenue	Construction Fund	Other Governmental Funds	Total Governmental Funds
Revenues:					
From local sources:					
Taxes:					
Property	\$ 2,222,775	\$ -	\$ -	\$ 369,189	\$ 2,591,964
Motor vehicle	500,645				500,645
Utilities	808,473				808,473
Other taxes	10,018				10,018
Earnings on investments	176,736	4,467	18,884	15,084	215,171
Other local revenues	255,930	16,991			272,921
Intergovernmental - State	14,093,915	953,269		1,094,251	16,141,435
Intergovernmental - Indirect Federal	71,763	2,520,016			2,591,779
Intergovernmental - Direct Federal	158,231	46,780			205,011
Total Revenues	18,298,486	3,541,523	18,884	1,478,524	23,337,417
Expenditures:					
Instruction	11,172,898	2,578,099			13,750,997
Support services:					
Student	1,272,514	76,429			1,348,943
Instruction staff	966,719	494,316			1,461,035
District administrative	698,441				698,441
School administrative	1,133,923	13,143			1,147,066
Business	604,960				604,960
Plant operation and maintenance	1,869,702				1,869,702
Student transportation	1,734,790	15,654			1,750,444
Facilities acquisition and construction			2,761,939		2,761,939
Community service activities		347,755			347,755
Bond issue costs			41,904		41,904
Debt service:					
Principal				714,191	714,191
Interest				741,332	741,332
Total Expenditures	19,453,947	3,525,396	2,803,843	1,455,523	27,238,709
Excess (Deficit) of Revenues over Expenditures	(1,155,461)	16,127	(2,784,959)	23,001	(3,901,292)
Other Financing Sources (Uses):					
Proceeds from sale of bonds	353,481		6,720,000		7,073,481
Bond discount			(48,365)		(48,365)
Proceeds from sale of fixed assets	6,611				6,611
Operating transfers in		35,320	193,628	1,009,150	1,238,098
Operating transfers out	(228,948)		(144,554)	(1,009,150)	(1,382,652)
Total Other Financing Sources	131,144	35,320	6,720,709	-	6,887,173
Excess (Deficit) of Revenue and Other Financing Sources over Expenditures and Other Financing Uses	(1,024,317)	51,447	3,935,750	23,001	2,985,881
Fund Balance, July 1, 2004	3,341,719	148,683	2,074,372	411,408	5,976,182
Fund Balance, June 30, 2005	\$ 2,317,402	\$ 200,130	\$ 6,010,122	\$ 434,409	\$ 8,962,063

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

Year Ended June 30, 2005

Net change in total fund balances per fund financial statements	\$ 2,985,881
Amounts reported for governmental activities in the statement of activities are different because:	
Capital outlays are reported as expenditures in this fund financial statement because they use current financial resources, but they are presented as assets in the statement of activities and depreciated over their estimated economic lives. The difference is the amount by which capital outlays exceed depreciation expense for the year.	2,299,699
The proceeds for the issuance of bonds provide current financial resources and are reported in this fund financial statement but they are presented as liabilities in the statement of net assets.	(6,983,212)
Bond and capital lease payments are recognized as expenditures of current financial resources in the fund financial statement but are reductions of liabilities in the statement of net assets.	853,468
In the statement of activities, only the gain (loss) on sale of fixed assets is reported, whereas in the governmental funds, the proceeds for the sale increased financial resources.	(1,893)
Generally, expenditures recognized in this fund financial statement are limited to only those that use current financial resources, but expenses are recognized in the statement of activities when they are incurred.	<u>49,347</u>
Change in net assets of governmental activities	<u>\$ (796,710)</u>

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF NET ASSETS

PROPRIETARY FUNDS

June 30, 2005

	Food Service Fund	FRC Childcare Fund	Total
Assets			
<u>Current Assets</u>			
Cash and cash equivalents	\$ -	\$ 15,341	\$ 15,341
Inventory	21,163		21,163
Due from other funds	33	19	52
Total Current Assets	21,196	15,360	36,556
<u>Noncurrent Assets</u>			
Capital assets	1,531,375		1,531,375
Less: accumulated depreciation	(461,814)		(461,814)
Total Noncurrent Assets	1,069,561	-	1,069,561
Total Assets	\$ 1,090,757	\$ 15,360	\$ 1,106,117
Liabilities			
<u>Current Liabilities</u>			
Accounts payable	\$ 2,646	\$ -	\$ 2,646
Cash overdraft	18,550		18,550
Due to other funds	10,086		10,086
Total Current Liabilities	31,282	-	31,282
<u>Net Assets</u>			
Invested in capital assets, net of related debt	1,069,561		1,069,561
Unrestricted	(10,086)	15,360	5,274
Total Net Assets	\$ 1,059,475	\$ 15,360	\$ 1,074,835

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUNDS

Year Ended June 30, 2005

	Food Service Fund	FRC Childcare	Total
Operating Revenues:			
Lunchroom sales	\$ 342,944	\$ -	\$ 342,944
Other operating revenues	24,436	64,369	88,805
Total Operating Revenues	367,380	64,369	431,749
Operating Expenses:			
Salaries and wages	623,757	63,992	687,749
Materials and supplies	692,107		692,107
Depreciation	54,361		54,361
Other operating expenses	14,959	12,281	27,240
Total Operating Expenses	1,385,184	76,273	1,461,457
Operating loss	(1,017,804)	(11,904)	(1,029,708)
Non-Operating Revenues (Expenses):			
Federal grants	804,865		804,865
Donated commodities	65,174		65,174
State grants	17,717	11,542	29,259
Loss on disposal of assets	(16,854)		(16,854)
Interest income	707		707
Total Non-Operating Revenues (Expenses) Before Transfers	871,609	11,542	883,151
Transfers in	144,554		144,554
Change in net assets	(1,641)	(362)	(2,003)
Net Assets, July 1, 2004	1,061,116	15,722	1,076,838
Net Assets, June 30, 2005	\$ 1,059,475	\$ 15,360	\$ 1,074,835

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF CASH FLOWS

PROPRIETARY FUNDS

Year Ended June 30, 2005

	Food Service Fund	FRC Childcare Fund	Total
Cash Flows from Operating Activities			
Cash received from:			
Lunchroom sales	\$ 342,944	\$ -	\$ 342,944
Other activities	24,436	67,291	91,727
Cash paid to/for:			
Employees	623,757	64,011	687,768
Supplies	618,422		618,422
Other activities	14,959	12,281	27,240
Net Cash (Used) by Operating Activities	(889,758)	(9,001)	(898,759)
Cash flows from Non-Capital and Related Financing Activities			
Federal grants	820,281		820,281
State grants	17,717	11,542	29,259
Transfers from other funds	144,554		144,554
Net Cash Provided by Non-Capital and Related Financing Activities	982,552	11,542	994,094
Cash Flows from Capital and Related Financing Activities			
Purchases of capital assets	(153,474)		(153,474)
Cash Flows from Investing Activities			
Receipt of interest income	707		707
Net increase (decrease) in cash and cash equivalents	(59,973)	2,541	(57,432)
Balances, beginning of year	41,423	12,800	54,223
Balances, end of year	<u>\$ (18,550)</u>	<u>\$ 15,341</u>	<u>\$ (3,209)</u>
Reconciliation of operating loss to net cash used by operating activities			
Operating loss	\$ (1,017,804)	\$ (11,904)	\$ (1,029,708)
Adjustments to reconcile operating loss to net cash (used) by operating activities:			
Depreciation	54,361		54,361
Donated commodities	65,174		65,174
Change in assets and liabilities:			
Accounts receivable		2,922	2,922
Due from other funds	(33)	(19)	
Inventory	(4,188)		(4,188)
Accounts payable	2,646		2,646
Due to other funds	10,086		10,086
Net cash used by operating activities	<u>\$ (889,758)</u>	<u>\$ (9,001)</u>	<u>\$ (898,707)</u>
Schedule of non-cash transactions:			
Donated commodities received from federal government	<u>\$ 65,174</u>	<u>\$ -</u>	<u>\$ 68,024</u>

See accompanying notes to financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENTS OF FIDUCIARY NET ASSETS

FIDUCIARY FUNDS

June 30, 2005

	Agency Fund
Assets	
Cash and cash equivalents	\$ 179,475
Accounts receivable	972
Total Assets	<u>\$ 180,447</u>
Liabilities	
Accounts payable	\$ 12,359
Due to student groups	168,088
Total Liabilities	<u>\$ 180,447</u>

See accompanying notes to financial statements.

NOTES TO THE BASIC FINANCIAL STATEMENTS

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Russell County Board of Education ("Board"), a five-member group, is the level of government, which has oversight responsibilities over all activities related to public elementary and secondary school education within the jurisdiction of Russell County Board of Education ("District"). The District receives funding from Local, State and Federal government sources and must comply with the commitment requirements of these funding source entities. However, the District is not included in any other governmental "reporting entity" as defined in Section 2100, Codification of Governmental Accounting and Financial Reporting Standards. Board members are elected by the public and have decision making authority, the power to designate management, the responsibility to develop policies, which may influence operations and primary accountability for fiscal matters. As allowed in Section P80 of GASB's Codification of Governmental Accounting and Financial Reporting Standards, the District has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedure issued after November 30, 1989.

The District, for financial purposes, includes all of the funds and account groups relevant to the operation of the Russell County Board of Education. The financial statements presented herein do not include funds of groups and organizations, which although associated with the school system, have not originated within the Board itself such as Band Boosters, Parent-Teacher Associations, etc.

The financial statements of the District include those of separately administered organizations that are controlled by or dependent on the Board. Control or dependence is determined on the basis of budget adoption, funding and appointment of the respective governing board.

Based on the foregoing criteria, the financial statements of the following organization are included in the accompanying financial statements:

Russell County Board of Education Finance Corporation – In a prior year, the Board of Education resolved to authorize the establishment of the Russell County School District Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Bond Act and KRS 273 and KRS Section 58.180) (the "Corporation") as an agency for the District for financing the costs of school building facilities. The members of the Board also comprise the Corporation's Board of Directors. The Corporation is blended into the District's financial statements.

Basis of Presentation

The District's basic financial statements consist of government-wide statements, including a statement of net assets and a statement of activities, and fund financial statements, which provide a more detailed level of financial information.

Government-wide Financial Statements – The statement of net assets and the statement of activities display information about the District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The statements distinguish between those activities of the District that are governmental and those that are considered business-type activities.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of the proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

The statement of net assets presents the financial condition of the governmental and business-type activities of the District at year-end. The statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the District and for each function or program of the District's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the District, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each business segment or governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements – Fund financial statements report detailed information about the District. The focus of governmental and enterprise fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. Fiduciary funds are reported by fund type.

The accounting and reporting treatment applied to a fund is determined by its measurement focus. All governmental fund types are accounted for using a flow of current financial resources measurement focus. The financial statements for governmental funds are a balance sheet, which generally includes only current assets and current liabilities, and a statement of revenues, expenditures and changes in fund balances, which reports on the changes in fund balances. Proprietary funds are reported using the economic resources measurement focus. All assets and liabilities associated with the operation of these funds are included on the statement of net assets. The statement of changes in fund net assets presents increases and decreases in net total assets. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary activities. Fiduciary funds are also reported using the economic resources measurement focus.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

The District has the following funds:

I. Governmental Fund Types

- (A) The General Fund is the main operating fund of the Board. It accounts for financial resources used for general types of operations. This is a budgeted fund, and any fund balances are considered as resources available for use. This is a major fund of the District.
- (B) The Special Revenue Fund accounts for proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to disbursements for specified purposes. It includes federal financial programs where unused balances are returned to the grantor at the close of the specified project periods as well as the state grant programs. Project accounting is employed to maintain integrity for the various sources of funds. The separate projects of federally-funded grant programs are identified in the Schedule of Expenditures of Federal Awards included in this report on pages 42 through 43. This is a major fund of the District.
- (C) Capital Project Funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities and equipment (other than those financed by Proprietary Fund).
 - 1. The Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund receives those funds designated by the state as Capital Outlay Funds and is restricted for use in financing projects identified in the District's facility plan.
 - 2. The Facility Support Program of Kentucky (FSPK) accounts for funds generated by the building tax levy required to participate in the School Facilities Construction Commission's construction funding and state matching funds, where applicable. Funds may be used for projects identified in the District's facility plan.
 - 3. The Construction Fund accounts for proceeds from sales of bonds and other revenues to be used for authorized construction. This is a major fund of the District.
- (D) The Debt Service Funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest and related cost; and for the payment of interest on general obligation notes payable, as required by Kentucky Law.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

II. Proprietary Fund Types (Enterprise Fund)

- A. The Food Service Fund is used to account for school food service activities, including the National School Lunch and Breakfast Programs, which are conducted in cooperation with the U.S. Department of Agriculture (USDA). Amounts have been recorded for in-kind contribution of commodities from the USDA. The Food Service Fund is a major fund.
- B. The FRC Childcare Fund is used to account for the District's childcare operation.

III. Fiduciary Fund Type (Agency Fund)

- A. The Agency fund accounts for activities of student groups and other types of activities requiring clearing accounts. These funds are accounted for in accordance with the Uniform Program of Accounting for School Activity Funds. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.

Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Proprietary and fiduciary funds also use the accrual basis of accounting.

Revenues – Exchange and Non-exchange Transactions – Revenues resulting from exchange transactions, in which each party receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recorded in the fiscal year in which the resources are measurable and available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the District, available means expected to be received within sixty days of the fiscal year-end.

Nonexchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the District must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. On a modified accrual basis, revenues from nonexchange transactions must also be available before it can be recognized.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Basis of Accounting - continued

Deferred Revenue – Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied.

Grants and entitlements received before the eligibility requirements are met are recorded as deferred revenue.

Expenses/Expenditures – On the accrual basis of accounting, expenses are recognized at the time they are incurred. The fair value of donated commodities used during the year is reported in the statement of revenues, expenses, and changes in net assets as an expense with a like amount reported as donated commodities revenue. Unused donated commodities are reported as deferred revenue.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation, are not recognized in governmental funds.

Property Taxes

Property Tax Revenues – Property taxes are normally levied each September on the assessed value listed as of the prior January 1, for all real and personal property in the county. The billings are considered due upon receipt by the taxpayer; however, the actual date is based on a period ending 30 days after the tax bill mailing. Property taxes collected are recorded as revenues in the fiscal year for which they were levied. All taxes collected are initially deposited into the General Fund and then transferred to the appropriate fund. The usual collection date is the period from November 1 through December 31. Property tax bills paid prior to December 1 received a two percent discount. Property taxes received after December 31, are considered to be delinquent and the County Attorney can file a lien against the property.

The property tax rates assessed for the year ended June 30, 2005, to finance operations were \$.423 per \$100 valuation for real property, \$.437 per \$100 valuation for business personal property and \$.525 per \$100 valuation for motor vehicles.

The District levies a utility gross receipts license tax in the amount of 3% of the gross receipts derived from the furnishings, within the county, of telephonic and telegraphic communications services, cablevision services, electric power, water, and natural, artificial and mixed gas.

Capital Assets

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported both in the business-type activities column of the government-wide statement of net assets and in the respective funds.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. The District maintains a capitalization threshold of one thousand dollars with the exception of computers, digital cameras and real property for which there is no threshold. The District does not possess any infrastructure. Improvements are capitalized; the cost of, normal maintenance and repairs that do not add to the value of the asset or materially extend an assets life are not.

All reported capital assets are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives for both general capital assets and proprietary fund assets:

<u>Description</u>	<u>Governmental Activities Estimated Lives</u>
Land improvements	20 years
Buildings and improvements	25-50 years
Technology equipment	5 years
Vehicles	5-10 years
General equipment	5-15 years
Food service equipment	5-12 years

Interfund Balances

On fund financial statements, receivables and payables resulting from short-term interfund loans are classified as "interfund receivables/payables". These amounts are eliminated in the governmental and business-type activities columns of the statements of net assets, except for the net residual amounts due between governmental and business-type activities, which are presented as internal balances.

Budgetary Process

Budgetary Basis of Accounting: The District's budgetary process accounts for certain transactions on a basis other than Generally Accepted Accounting Principles (GAAP). The major differences between the budgetary basis and the GAAP basis are:

Revenues are recorded when received in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

Expenditures are recorded when paid in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

Once the budget is approved, it can be amended. Amendments are presented to the Board at their regular meetings. All budget appropriations lapse at year-end.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Encumbrances

Encumbrances are not liabilities and, therefore, are not reported as expenditures until receipt of material or service. For budgetary purposes, appropriations lapse at fiscal year-end and outstanding encumbrances at year-end are reappropriated in the next year. A reservation of fund balance equal to outstanding encumbrances at year-end is provided for at June 30, 2005.

Cash and Cash Equivalents

The District considers demand deposits, money market funds, and other investments with an original maturity of 90 days or less, to be cash equivalents.

Inventories

On government-wide financial statements inventories are stated at cost and are expensed when used.

On fund financial statements inventories are stated at cost. The cost of inventory items is recorded as an expenditure in the governmental fund types when purchased.

The food service fund uses the specific identification method and the general fund uses the first-in, first-out method.

Prepaid Assets

Payments made that will benefit periods beyond June 30, 2005, are recorded as prepaid items using the consumption method. A current asset for the prepaid amount is recorded at the time of the purchase and an expenditure/expense is reported in the year in which services are consumed.

Receivables

The District recognizes revenues as receivable when they are measurable and receipt is probable. Concentration of credit risk with respect to the receivables from federal and state governments is limited due to the historical stability of those institutions.

Accrued Liabilities and Long-Term Obligations

All payables accrued liabilities and long-term obligations are reported in the government-wide financial statements, and all payables, accrued liabilities and long-term obligations payable from proprietary funds are reported on the proprietary fund financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

In general, payables and accrued liabilities that will be paid from governmental funds are reported on the governmental fund financial statements regardless of whether they will be liquidated with current resources. However, claims and judgments, the noncurrent portion of capital leases, accumulated sick leave, contractually required pension contributions and special termination benefits that will be paid from governmental funds are reported as a liability in the fund financial statements only to the extent that they will be paid with current, expendable, available financial resources. In general, payments made within sixty days after year-end are considered to have been made with current available financial resources. Bonds and other long-term obligations that will be paid from governmental funds are not recognized as a liability in the fund financial statements until due.

Fund Balance Reserves

The District reserves those portions of fund equity which are legally segregated for a specific future use or which do not represent available expendable resources and therefore are not available for appropriation or expenditure. Unreserved fund balance indicates that portion of fund equity, which is available for appropriation in future periods. Fund equity reserves have been established for SFCC escrow and debt service.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the School District or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the School District, those revenues are primarily charges for meals provided by the various schools and for childcare services provided.

Contributions of Capital

Contributions of capital in proprietary fund financial statements arise from outside contributions of fixed assets, or from grants or outside contributions of resources restricted to capital acquisition and construction.

Interfund Activity

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and after nonoperating revenues/expenses in proprietary funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE B – ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the District's management to make estimates and assumptions that affect reported amounts of assets, liabilities, fund balances, and disclosure of contingent assets and liabilities at the date of the general purpose financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

NOTE C – CASH AND CASH EQUIVALENTS

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District's policy is to have all deposits secured by pledged securities. At June 30, 2005, none of the District's bank balance of \$11,503,746 was exposed to custodial credit risk.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE D - CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2005, was as follows:

Governmental Activities	Balance July 1, 2004	Additions	Deductions	Balance June 30, 2005
Non-Depreciable Assets:				
Land	\$ 592,322	\$ -	\$ -	\$ 592,322
Construction in progress	4,267,323	2,696,412	(6,325,677)	638,058
Depreciable Assets:				
Land improvements	1,453,896			1,453,896
Buildings and improvements	22,401,429	6,325,677	(110,837)	28,616,269
Technology equipment	1,151,586	212,512	(117,346)	1,246,752
Vehicles	3,288,111	362,481	(235,190)	3,415,402
General equipment	631,351	36,665	(1,299)	666,717
Totals at historical cost	33,786,018	9,633,747	(6,790,349)	36,629,416
Accumulated depreciation:				
Land improvements	786,808	67,952		854,760
Buildings and improvements	6,281,152	582,087	(110,837)	6,752,402
Technology equipment	900,726	140,432	(116,274)	924,884
Vehicles	2,305,086	168,827	(234,368)	2,239,545
General equipment	331,483	48,867	(1,299)	379,051
Total accumulated depreciation	10,605,255	1,008,165	(462,778)	11,150,642
Government Activities Capital Assets - Net	<u>\$ 23,180,763</u>	<u>\$ 8,625,582</u>	<u>\$ (6,327,571)</u>	<u>\$ 25,478,774</u>
Business-Type Activities				
Buildings and improvements	\$ 1,118,055		\$ (80,894)	\$ 1,037,161
Food service equipment	355,699	153,474	(14,959)	494,214
Totals at historical cost	1,473,754	153,474	(95,853)	1,531,375
Accumulated depreciation:				
Buildings and improvements	255,766	20,878	(64,040)	212,604
Food service equipment	230,686	33,483	(14,959)	249,210
Total accumulated depreciation	486,452	54,361	(78,999)	461,814
Government Activities Capital Assets - Net	<u>\$ 987,302</u>	<u>\$ 99,113</u>	<u>\$ (16,854)</u>	<u>\$ 1,069,561</u>
Depreciation was charged to governmental functions as follows:				
Instruction	\$ 807,696			
Student support	260			
Instructional staff	599			
District administration	13,447			
School administration	1,491			
Plant	31,399			
Transportation	149,460			
Community services	3,813			
	<u>\$ 1,008,165</u>			

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE E – LONG-TERM OBLIGATIONS

The original amount of each issue, the issue date, and interest rates are summarized below:

<u>Issue Date</u>	<u>Proceeds</u>	<u>Rates</u>
1998	\$ 925,000	3.95% - 4.60%
2000	4,900,000	5.25% - 5.62%
2002	4,900,000	1.40% - 4.10%
2003	6,355,000	2.50% - 4.10%
2005	6,720,000	3.50% - 4.20%

On June 1, 2005, the District issued \$6,720,000 in 2005 Series Revenue Bonds with an average interest rate of 3.73 percent for the improvements at Salem and Union Chapel Elementary Schools. The net proceeds of \$6,644,686 (after \$41,904 in cost of issuance and \$48,365 of discount and \$14,955 in accrued interest) were deposited; \$6,184,350 in the Construction Fund and \$14,955 in the Debt Service Fund.

The District, through the General Fund (including utility taxes and the Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund) is obligated to make payments in amounts sufficient to satisfy debt service requirements on bonds issued by the Russell County School District Finance Corporation to construct school facilities. The District has an option to purchase the property under lease at any time by retiring the bonds then outstanding.

The District has "participation agreements" with the Kentucky School Facilities Construction Commission. The Commission was created by the Kentucky General Assembly for the purpose of assisting local school districts in meeting school construction needs. The table below sets forth the amount to be paid by the District and the Commission for each year until maturity of all bond issues. The liability for the total bond amount remains with the District and, as such, the total principal outstanding has been recorded in the financial statements.

The bonds may be called prior to maturity and redemption premiums are specified in each issue. Assuming no bonds are called prior to scheduled maturity, the minimum obligations of the District, including amounts to be paid by the Commission, at June 30, 2005, for debt service (principal and interest) are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Participation</u>	<u>District's Portion</u>
2005-06	\$ 890,000	\$ 923,616	\$ 336,476	\$ 1,477,140
2006-07	900,000	895,432	336,949	1,458,483
2007-08	895,000	866,143	305,297	1,455,846
2008-09	925,000	834,642	301,764	1,457,878
2009-10	855,000	800,912	200,749	1,455,163
2011-15	4,730,000	3,494,840	940,882	7,283,958
2016-20	5,285,000	2,409,082	547,381	7,146,701
2021-25	6,280,000	1,005,248	130,423	7,154,825
2025-26	855,000	21,375	-	876,375
	<u>\$ 21,615,000</u>	<u>\$11,251,290</u>	<u>\$ 3,099,921</u>	<u>\$ 29,766,369</u>

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE E – LONG-TERM OBLIGATIONS - CONTINUED

Accumulated Unpaid Sick Leave Benefits

Upon retirement from the school system, an employee will receive from the District an amount equal to 30% of the value of accumulated sick leave.

Sick leave benefits are accrued as a liability using the termination payment method. An accrual for earned sick leave is made to the extent that it is probable that the benefits will result in termination payments. The liability is based on the School District's past experience of making termination payments.

The entire compensated absence liability is reported on the government-wide financial statements.

For governmental fund financial statements the current portion of unpaid accrued sick leave is the amount expected to be paid using expendable available resources. These amounts are recorded in the account "accumulated sick leave payable" in the general fund. The noncurrent portion of the liability is not reported.

Long-term liability for the year ended June 30, 2005, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Amounts Due Within One Year</u>
Governmental Activities:					
Revenue bonds payable	\$15,550,000	\$6,720,000	\$655,000	\$21,615,000	\$890,000
Accrued sick leave	<u>1,013,798</u>	<u>132,860</u>	<u>165,857</u>	<u>980,801</u>	<u>103,969</u>
Governmental Activities:					
Long-term liabilities	<u>\$15,563,798</u>	<u>\$6,852,860</u>	<u>\$815,857</u>	<u>\$22,595,801</u>	<u>\$993,969</u>

The debt service fund is primarily responsible for paying the bond obligations through funding from the capital outlay and FSPK funds. The general fund is primarily responsible for paying accrued sick leave.

NOTE F – CAPITAL LEASE PAYABLE

The following is an analysis of the leased property under capital lease by class:

<u>Classes of Property</u>	<u>Book value as of June 30, 2005</u>
Buses and garbage truck	\$ 889,773
School Improvements	1,095,588

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE F – CAPITAL LEASE PAYABLE - CONTINUED

The following is a schedule by years of the future minimum lease payments under capital lease together with the present value of the net minimum lease payments as of June 30, 2005:

<u>Year Ending June 30,</u>	<u>Capital Lease Payable</u>
2006	\$ 336,986
2007	303,491
2008	294,685
2009	290,590
2010	286,011
2011-2015	1,021,454
2016-2019	<u>433,846</u>
Total minimum lease payments	2,967,063
Less: Amount representing interest	<u>(626,922)</u>
Present Value of Net Minimum Lease Payments	\$ <u>2,161,680</u>

In January 2005, the District entered into a new lease for four buses and a garbage truck for \$353,481.

NOTE G – COMMITMENTS UNDER NONCAPITALIZED LEASES

Commitments under operating lease agreements for office equipment provide the minimum future rental payments as of June 30, 2005 as follows:

<u>Year Ending June 30,</u>	
2006	\$ 17,268
2007	<u>771</u>
	<u>\$ 18,039</u>

Rent expense for the year ended June 30, 2005 was \$27,274.

NOTE H – RETIREMENT PLANS

All the District's eligible employees participate in the Kentucky Teacher's Retirement System (KTRS), a statewide multiple-employer public employee retirement system covering all employees of local school districts within the State of Kentucky. KTRS is a cost sharing public employee retirement system with one exception: all risks and costs are not shared by the District but are the liability of the State of Kentucky. KTRS is funded through state and employee contributions and the District has no legal obligation for paying benefits. As discussed below, the District may be required in certain situations to make limited contributions on behalf of certain employees.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE H – RETIREMENT PLANS – CONTINUED

The State of Kentucky contributes 13.105% of the employee's gross earnings except for those District employees being paid from and participating in federally funded programs. During the year, contributions of \$1,351,691 were made by the State of Kentucky and \$168,311 in contributions were passed through the District's federally funded programs. Contributions by the employees are 9.855% of gross earnings and are withheld by the District. Such withholdings totaled \$1,143,064 during the year and were paid by the District to the State of Kentucky. The District has no other liability under the plan. The District's total payroll for all employees during the year was \$15,342,669, and \$11,598,641 of such amount related to employees covered by the retirement plan.

Substantially all other employees (classified personnel) are covered under the County Employee's Retirement System (CERS). Funding for the Plan is provided through payroll withholdings of 5% and a District contribution of 7.34% of the employee's total compensation subject to contribution. The District's contribution requirement for CERS for the year ended June 30, 2005 was \$468,986, which consisted of \$295,028 from the District and \$173,958 from the employees. The total covered payroll for CERS during the year was \$3,479,104. Benefits under both plans will vary based on final compensation, years of service and other factors as fully described in the Plan documents.

Additional information and historical trend information can be obtained from the separately issued Teacher Retirement System of Kentucky Comprehensive Annual Financial Report.

Deferred Compensation

The District offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The Plan, available to all employees, permits them to defer a portion of their salary until future years. This deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency. GASB Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, allows entities with little or no administrative involvement who do not perform the investing function for these plans to omit plan assets and related liabilities from their financial statements. The Board therefore does not show these assets and liabilities on this financial statement.

NOTE I - CONTINGENCIES

The District receives funding from Federal, State and Local government agencies and private contributions. These funds are to be used for designated purposes only. For government agency grants, if based upon the grantor's review, the funds are considered not to have been used for the intended purpose, the grantors may request a refund of monies advanced, or refuse to reimburse the District for its disbursements. The amount of such future refunds and unreimbursed disbursements, if any, is not expected to be significant. Continuation of the District's grant programs is predicated upon the grantors' satisfaction that the funds provided are being spent as intended and the grantors' intent to continue their programs.

NOTE J - LITIGATION

The District is subject to various other legal actions in various stages of litigation, the outcome of which is not determinable at this time. Management of the District and its legal counsel do not anticipate that there will be any material effect on the combined financial statements as a result of the cases presently in progress, except as described elsewhere in this report.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE K - INSURANCE AND RELATED ACTIVITIES

The District is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. Each of these risk areas is covered through the purchase of commercial insurance. The District has purchased certain policies, which are retrospectively rated which includes Workers' Compensation insurance.

NOTE L - RISK MANAGEMENT

The District is exposed to various risks of loss related to injuries to employees. To obtain insurance of workers' compensation, errors and omissions, and general liability coverage, the District participates in the Kentucky School Boards Insurance Trust Liability Insurance Fund. The public entity risk pools operate as common risk management and insurance programs for all school district and other tax supported educational agencies of Kentucky who are members of the Kentucky School Boards Association. The District pays an annual premium to each fund for coverage. Contributions to the Workers' Compensation fund are based on premium rates established by such fund in conjunction with the excess insurance carrier, subject to claims experience modifications and a group discount amount. Dividends may be declared, but are not payable until twenty-four (24) months after the expiration of the self-insurance term. The Liability Insurance fund pays insurance premiums of the participating members established by the insurance carrier. The Trust can terminate coverage if it is unable to obtain acceptable excess general liability coverage and for any reason by giving ninety (90) days notice. In the event the Trust terminated coverage, any amount remaining in the Fund (after payment of operational and administrative costs and claims for which coverage was provided) would be returned to the members on a pro rata basis.

The District purchases unemployment insurance through the Kentucky School Boards Insurance Trust Unemployment Compensation Fund; however, risk has not been transferred to such fund. In addition, the District continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE M - DEFICIT OPERATING BALANCES

There are no funds of the District that currently have a deficit fund balance/net assets. However, the following funds have operations that resulted in a current year deficit of revenues over expenditures resulting in a corresponding reduction of fund balance/net assets:

General Fund	\$ 1,024,460
Capital Outlay Fund	158,545
Food Service	1,641
FRC Childcare	362

NOTE N - COBRA

Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement may put the School District at risk for a substantial loss (contingency).

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED

June 30, 2005

NOTE O - TRANSFER OF FUNDS

The following transfers were made during the year:

<u>Type</u>	<u>From Fund</u>	<u>To Fund</u>	<u>Purpose</u>	<u>Amount</u>
Operating	General	Special Revenue	Technology Match	\$ 35,320
Operating	General	Construction	Construction	193,628
Operating	SEEK Capital Outlay	Debt Service	Debt Service	417,045
Operating	FSPK Fund	Debt Service	Debt Service	592,105

NOTE P – INTERFUND RECEIVABLES AND PAYABLES

Interfund balances at June 30, 2005 consisted of the following individual fund receivables and payables:

	<u>Receivables</u>	<u>Payables</u>
General Fund	\$ 10,086	\$ 5,599
Special Revenue Fund	5,547	
Food Service Fund	33	10,086
FRC Childcare	19	
	<u>\$ 15,685</u>	<u>\$ 15,685</u>

These items were for amounts due that were paid by the receivable fund for the payable fund. These balances were eliminated in the government wide financial statements with only the payables between the governmental and business-type funds being included.

NOTE Q – ON-BEHALF PAYMENTS

The District receives on-behalf payments from the State of Kentucky for items including retirement and insurance. The amount received for the fiscal year ended June 30, 2005, was \$3,524,575.

NOTE R – BUILDING LEASE

The District leases a portion of its Learning Center to various entities. The following represents payments to be received.

<u>Year Ending</u> <u>June 30,</u>	<u>Amount to</u> <u>be Received</u>
2006	\$ 23,871
2007	<u>23,871</u>
	<u>\$ 47,742</u>

NOTE S – PRIOR PERIOD ADJUSTMENT

The District decreased the beginning fund balance for the Debt Service Fund by \$40,100 for expenditures made in the prior year. There was no effect on revenues or expenditures of the current year.

REQUIRED SUPPLEMENTARY INFORMATION

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE- BUDGET AND ACTUAL

GENERAL FUND

Year Ended June 30, 2005

	<u>Original</u>	<u>Final</u>	<u>Actual</u>
Revenues:			
From local sources:			
Taxes:			
Property	\$ 1,720,482	\$ 1,565,000	\$ 2,222,775
Motor vehicle	450,000	450,000	500,645
Utilities	600,000	600,000	808,473
Other taxes			10,018
Earnings on investments	150,000	150,000	176,736
Other local revenues			255,930
Intergovernmental - State	10,665,000	10,649,000	14,093,915
Intergovernmental - Indirect Federal			71,763
Intergovernmental - Direct Federal			158,231
Total Revenues	<u>13,585,482</u>	<u>13,414,000</u>	<u>18,298,486</u>
Expenditures:			
Instruction	8,497,065	8,553,926	11,172,898
Support services:			
Student	1,019,010	1,009,118	1,272,514
Instruction staff	656,919	816,752	966,719
District administrative	1,170,056	1,171,184	698,441
School administrative	854,427	874,168	1,133,923
Business	224,055	228,115	604,960
Plant operation and maintenance	1,623,112	2,526,418	1,869,702
Student transportation	1,375,063	1,387,163	1,734,790
Central office	180,639	188,872	
Total Expenditures	<u>15,600,346</u>	<u>16,755,716</u>	<u>19,453,947</u>
Excess (Deficit) of Revenues over Expenditures	<u>(2,014,864)</u>	<u>(3,341,716)</u>	<u>(1,155,461)</u>
Other Financing Sources (Uses):			
Proceeds from sale of bonds			353,481
Proceeds from sale of fixed assets			6,611
Operating transfers out			(228,948)
Total Other Financing Sources	<u>-</u>	<u>-</u>	<u>131,144</u>
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	<u>(2,014,864)</u>	<u>(3,341,716)</u>	<u>(1,024,317)</u>
Fund balance, July 1, 2004	<u>2,014,864</u>	<u>3,341,716</u>	<u>3,341,719</u>
Fund balance, June 30, 2005	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,317,402</u>

Both inflows and outflows are equally different in the Statement of Revenues, Expenditures and Changes in Fund Balances Governmental Funds by the amount of on-behalf payments of \$3,524,575.

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE- BUDGET AND ACTUAL

SPECIAL REVENUE FUND

Year Ended June 30, 2005

	<u>Original</u>	<u>Final</u>	<u>Actual</u>
Revenues:			
Earnings on investments	\$ -	\$ -	\$ 4,467
Other local revenues	14,974	16,991	16,991
Intergovernmental - State	846,731	968,002	953,269
Intergovernmental - Indirect Federal	2,141,642	2,452,518	2,520,016
Intergovernmental - Direct Federal			46,780
Total Revenues	<u>3,003,347</u>	<u>3,437,511</u>	<u>3,541,523</u>
Expenditures:			
Instruction	2,066,621	2,470,312	2,578,099
Support services:			
Student	46,673	79,818	76,429
Instruction staff	355,190	536,573	494,316
Business		16,946	13,143
Student transportation	8,621	24,881	15,654
Community service activities	357,083	308,981	347,755
Total Expenditures	<u>2,834,188</u>	<u>3,437,511</u>	<u>3,525,396</u>
Excess (Deficit) of Revenues over Expenditures	169,159	-	16,127
Other Financing Sources (Uses):			
Operating transfers in			35,320
Total Other Financing Sources (Uses)	<u>-</u>	<u>-</u>	<u>35,320</u>
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	169,159		51,447
Fund balance, July 1, 2004	<u>-</u>	<u>-</u>	<u>148,683</u>
Fund balance, June 30, 2005	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 200,130</u>

SUPPLEMENTARY INFORMATION

RUSSELL COUNTY SCHOOL DISTRICT

COMBINING BALANCE SHEET - NONMAJOR GOVERNMENTAL FUNDS

June 30, 2005

	SEEK Capital Outlay Fund	FSPK Fund	Debt Service Fund	Total Nonmajor Governmental Funds
Assets and Resources:				
Cash and cash equivalents	\$ 192,708	\$ 226,747	\$ 14,954	\$ 434,409
Total Assets and Resources	<u>\$ 192,708</u>	<u>\$ 226,747</u>	<u>\$ 14,954</u>	<u>\$ 434,409</u>
Liabilities and Fund Balances:				
Liabilities				
Accounts payable	\$ -	\$ -	\$ -	\$ -
Total Liabilities				
Fund Balances				
Reserved for:				
SFCC escrow	192,708	226,747		419,455
Debt service			14,954	14,954
Total Fund Balances	<u>192,708</u>	<u>226,747</u>	<u>14,954</u>	<u>434,409</u>
Total Liabilities and Fund Balances	<u>\$ 192,708</u>	<u>\$ 226,747</u>	<u>\$ 14,954</u>	<u>\$ 434,409</u>

RUSSELL COUNTY SCHOOL DISTRICT

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS

Year Ended June 30, 2005

	SEEK Capital Outlay Fund	FSPK Fund	Debt Service Fund	Total Nonmajor Governmental Funds
Revenues				
From local sources:				
Taxes:				
Property	\$ -	\$ 369,189	\$ -	\$ 369,189
Earnings on investments			15,084	15,084
Intergovernmental - State	258,500	389,508	446,243	1,094,251
Total Revenues	258,500	758,697	461,327	1,478,524
Expenditures				
Debt service:				
Principal			714,191	714,191
Interest			741,332	741,332
Total Expenditures	-	-	1,455,523	1,455,523
Excess (Deficit) of Revenues over Expenditures	258,500	758,697	(994,196)	23,001
Other Financing Sources (Uses)				
Operating transfers in			1,009,150	1,009,150
Operating transfers out	(417,045)	(592,105)		(1,009,150)
Total Other Financing Sources (Uses)	(417,045)	(592,105)	1,009,150	-
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	(158,545)	166,592	14,954	23,001
Fund balance, July 1, 2004	351,253	60,155		411,408
Fund balance, June 30, 2005	\$ 192,708	\$ 226,747	\$ 14,954	\$ 434,409

RUSSELL COUNTY SCHOOL DISTRICT

COMBINING STATEMENT OF FIDUCIARY NET ASSETS

FIDUCIARY FUNDS

June 30, 2005

	Russell Springs Elementary	Union Chapel Elementary	Jamestown Elementary	Salem Elementary	Russell County Middle School	Russell County High School	Total Agency Fund
Assets							
Cash and cash equivalents	\$ 32,950	\$ 12,897	\$ 10,701	\$ 12,538	\$ 48,245	\$ 62,144	\$ 179,475
Accounts receivable						972	972
Total Assets	<u>\$ 32,950</u>	<u>\$ 12,897</u>	<u>\$ 10,701</u>	<u>\$ 12,538</u>	<u>\$ 48,245</u>	<u>\$ 63,116</u>	<u>\$ 180,447</u>
Liabilities							
Accounts payable	\$ 3,578	\$ 583	\$ 2,096	\$ -	\$ -	\$ 6,102	\$ 12,359
Due to student groups	29,372	12,314	8,605	12,538	48,245	57,014	168,088
Total Liabilities	<u>\$ 32,950</u>	<u>\$ 12,897</u>	<u>\$ 10,701</u>	<u>\$ 12,538</u>	<u>\$ 48,245</u>	<u>\$ 63,116</u>	<u>\$ 180,447</u>

RUSSELL COUNTY SCHOOL DISTRICT

STATEMENT OF RECEIPTS, DISBURSEMENTS, AND FUND BALANCES

RUSSELL COUNTY HIGH SCHOOL

FOR YEAR ENDED JUNE 30, 2005

NAME OF ACTIVITY	CASH BALANCES July 1, 2004	RECEIPTS	DISBURSEMENTS	CASH BALANCES June 30, 2005	ACCOUNTS RECEIVABLE June 30, 2005	ACCOUNTS PAYABLE June 30, 2005	DUE TO STUDENT GROUPS June 30, 2005
Agriculture (Shop)	\$ 2,134	\$ 19,654	\$ 13,464	\$ 8,324	\$ -	\$ 2,376	\$ 5,948
Art Club	673	1,113	1,585	201	-	-	201
Athletic	16,103	86,870	92,694	10,279	-	-	10,279
Boss	248	629	531	346	-	-	346
CAD	33	-	33	-	-	-	-
Chess Club	208	-	208	-	-	-	-
Concession	33,974	25,183	52,843	6,314	972	-	7,286
Drama	11	933	200	744	-	-	744
English	110	1,522	1,632	-	-	-	-
FBLA	1,784	1,105	1,387	1,502	-	-	1,502
FCA	675	868	1,085	458	-	62	396
FCCLA	2,272	3,986	5,770	488	-	-	488
Flower & Gift Fund	1,777	8,834	9,358	1,253	-	-	1,253
Fundraiser	1,174	890	2,064	-	-	27	(27)
Homecoming (Floats)	40	-	40	-	-	-	-
Horticulture	3,697	-	25	3,672	-	-	3,672
KTLN	146	-	146	-	-	-	-
Library	487	516	436	567	-	-	567
Miscellaneous	6,142	53,345	58,059	1,428	-	162	1,266
ROTC	6,448	16,585	17,468	5,565	-	3,361	2,204
Senior Class	203	49,677	48,790	1,090	-	14	1,076
Spanish	-	1,309	646	663	-	-	663
State Books	188	37	-	225	-	-	225
Student Council	621	-	108	513	-	-	513
Tech Ed	487	1,209	839	857	-	-	857
Teen Republican	-	-	-	-	-	-	-
Tri Hi	230	-	230	-	-	-	-
WLKR	105	495	-	600	-	-	600
Y-Club	198	2,846	2,672	372	-	-	372
Yearbook	6,932	25,822	16,071	16,683	-	100	16,583
TOTAL	\$ 87,100	\$ 303,428	\$ 328,384	\$ 62,144	\$ 972	\$ 6,102	\$ 57,014

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

RUSSELL COUNTY SCHOOL DISTRICT

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2005

<u>FEDERAL GRANTOR/PASS-THROUGH GRANTOR / PROGRAM TITLE</u>	<u>FEDERAL CFDA NUMBER</u>	<u>PASS THROUGH GRANTOR'S NUMBER</u>	<u>FEDERAL EXPENDITURES</u>
<u>U.S. DEPARTMENT OF AGRICULTURE</u>			
Passed Through State Department of Education:			
National School Lunch	10.555	* 575-04-02	\$ 124,780
		575-05-02	481,394
School Breakfast	10.553	* 576-04-05	44,260
		576-05-05	154,431
Summer Feeding Program	10.559	* 569-04-24	
Passed Through State Dept. of Agriculture			
Food Distribution (In-Kind Commodities)	10.555	* N/A	<u>65,174</u>
TOTAL U.S. DEPT. OF AGRICULTURE			<u>870,039</u>
<u>U.S. DEPARTMENT OF EDUCATION</u>			
Impact Aid	84.041	N/A	158,231
Passed Through State Department of Education:			
Title I	84.010	3104	203,585
		3105	786,368
Title I - Migrant	84.011	3114	2,690
		3115	66,569
Title IIC	84.048	3484A	1,344
		3485	23,307
IDEA - Part B	84.027	3374	78,183
		3375	449,744
IDEA - Part B - Preschool	84.173	3434	11,492
Title IV	84.186	4065	22,713
Innovative Program Strategies	84.298	3344	2,361
		3345	16,082
Rural and Low Income Schools	84.358B	3504	17,272
		3505	82,779
Teacher Quality	84.367A	* 4014	24,595
		4015	176,549
Title II D	84.318X	4254	93
		4255	23,111
		42553	24,983
21st Century Grant	84.287	* 5504	18,847
		5505	96,517
		5505D	124,154

* Denotes major federal program

The accompanying notes are an integral part of this schedule.

RUSSELL COUNTY SCHOOL DISTRICT

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - CONCLUDED

YEAR ENDED JUNE 30, 2005

<u>FEDERAL GRANTOR/PASS-THROUGH GRANTOR / PROGRAM TITLE</u>	<u>FEDERAL CFDA NUMBER</u>	<u>PASS THROUGH GRANTOR'S NUMBER</u>	<u>FEDERAL EXPENDITURES</u>
Passed Through Cabinet for Workforce Development Adult Basic Ed.	84.002	3655 3735	2,864 37,325
Education and Career Adv	84.002	3744 3745	15,094 70,785
Tech Prep	84.243	3635	9,500
TOTAL U.S. DEPARTMENT OF EDUCATION			2,547,137
<u>U.S. DEPARTMENT OF DEFENSE</u>			
ROTC	12.000	5045	46,780
TOTAL U.S. DEPARTMENT OF DEFENSE			46,780
<u>U.S. DEPARTMENT OF LABOR</u>			
Passed Through Lake Cumberland Community Services Organization, Inc. Workforce Investment Act	17.259	5885 5885A	30,000 80,147
Passed Through Cabinet for Workforce Development School to Careers	17.263	1775	17,964
TOTAL U.S. DEPARTMENT OF LABOR			128,111
<u>CORPORATION FOR NATIONAL AND COMMUNITY SERVICE</u>			
Passed Through State Department of Education: Learn and Serve	94.004	6755	3,000
TOTAL CORPORATION FOR NATIONAL AND COMMUNITY SERVICE			3,000
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$ 3,595,067

* Denotes major federal program

The accompanying notes are an integral part of this schedule.

RUSSELL COUNTY SCHOOL DISTRICT

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2005

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Russell County School District and is presented on the accrual basis of accounting for proprietary funds and the modified accrual basis of accounting for governmental funds. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

NOTE B – FOOD DISTRIBUTION

Nonmonetary assistance is reported in the schedule at the fair value of the commodities disbursed.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I-Summary of Auditor's Results

Section I-Summary of Auditor's Results

Section II – Financial Statement of Findings

No matters were reported.

Section III – Federal Award Findings and Questioned Costs

No matters were reported.

SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

RUSSELL COUNTY SCHOOL DISTRICT

SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

June 30, 2005

There were no prior year audit findings.

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

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Members of the Board of Education
Russell County School District
Jamestown, Kentucky

We have audited the basic financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Russell County Board of Education as of and for the year ended June 30, 2005, which collectively comprise the Russell County Board of Education's basic financial statements and have issued our report thereon dated September 23, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States and the audit requirements prescribed by the Kentucky State Committee for School District Audits in Appendices I, II and III of the Independent Auditor's Contract.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Russell County Board of Education's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Russell County Board of Education's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

We also noted certain additional matters that we have reported to the management of Russell County Board of Education in a separate letter dated September 23, 2005.

This report is intended for the information of members of the Kentucky State Committee for School District Audits, the members of the Board of Education of Russell County School District, the Kentucky Department of Education and management and should not be used by anyone other than these specified parties.

Stiles, Carter & Associates

Certified Public Accountants
September 23, 2005

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND
INTERNAL CONTROL OVER COMPLIANCE IN
ACCORDANCE WITH OMB CIRCULAR A-133**

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Compliance

We have audited the compliance of Russell County School District with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2005. Russell County School District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Russell County School District's management. Our responsibility is to express an opinion on Russell County School District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations and the audit requirements prescribed by the Kentucky State Committee for School District Audits in Appendices I, II and III of the Independent Auditor's Contract. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Russell County School District's compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Russell County School District's compliance with those requirements.

In our opinion, Russell County School District complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005.

Internal Control Over Compliance

The management of Russell County School District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Russell County School District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material

weaknesses. In addition, the results of our tests disclosed no instances of noncompliance of specific state statutes or regulations identified in Appendix II of the Independent Auditor's Contract - State Audit Requirements.

This report is intended for the information of members of the Kentucky State Committee for School District Audits, the members of the Board of Education of Russell County School District, the Kentucky Department of Education, management and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Hiles, Carter & Associates
Certified Public Accountants
September 23, 2005

MANAGEMENT LETTER COMMENTS

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In planning and performing our audit of the basic financial statements of Russell County School District for the year ended June 30, 2005, we considered the District's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters. A separate report dated September 23, 2005, contains our report on the District's internal control structure. This letter does not affect our report dated September 23, 2005, on the financial statements of the Russell County School District.

We will review the status of these comments during our next audit engagement. We have already discussed many of these comments and suggestions with various District personnel, and their implementation is currently being reviewed. We will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Stiles, Carter & Associates

Certified Public Accountants
September 23, 2005

RUSSELL COUNTY SCHOOL DISTRICT

MANAGEMENT LETTER COMMENTS

June 30, 2005

UNCORRECTED PRIOR YEAR COMMENTS

Bank Accounts

Only bank accounts authorized and approved by the Board should be established under the Board's federal identification number. We noted that several independent organizations have established bank accounts using the Board's federal identification number. These organizations include booster clubs, PTO's and other entities. We recommend that the Board contact these organizations and ensure that the bank accounts are not identified with the Board's federal identification number.

Management Response

The District will contact each entity and present the options for moving the accounts from the Board's identification number.

Segregation of Duties in Handling Receipts and Paying Bills – School Activity Funds

During our audit, we noted that Salem Elementary School did not comply with the segregation of duties requirements for handling receipts and paying bills as required by *Accounting Procedures for Kentucky School Activity Funds* issued by the Kentucky Department of Education. Russell County Middle School, Russell Springs Elementary School and Union Chapel Elementary School did not comply with the paying bills requirements.

Management Response

The District will meet with the schools to ensure that the procedures required by *Accounting Procedures for Kentucky School Activity Funds* issued by the Kentucky Department of Education are followed.

CURRENT YEAR COMMENTS

Organization of Invoices

During our audit, we noted that invoices were not consistently filed in the proper vendor file or there were multiple files established for the same vendor. This leads to unnecessary time devoted to locating invoices. We recommend that the District adopt a filing system that includes filing invoices by check number order.

Management Response

The District will review invoice filing procedures.

Food Service Budget

During our audit, we noted that the food service fund had not changed its budget for several years. The result was actual expenses significantly exceeding budgeted expenses. The failure to adequately budget and monitor the fund has led to large decreases in net assets during the preceding and current year. We recommend that the District closely monitor and budget this fund to improve operations.

Management Response

The District will ensure that an accurate budget is adopted and monitored.

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Russell County Board of Education
Jamestown, Kentucky

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Russell County School District as of and for the year ended June 30, 2005, which collectively comprise the District's basic financial statements, as listed in the accompanying table of contents, and have issued our report thereon dated September 23, 2005. Professional standards require that we provide you with the following information related to our audit.

Our responsibility under auditing standards generally accepted in the United States of America, the standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and the audit requirements prescribed by the Kentucky State Committee for School District Audits in Appendices I, II and III of the *Independent Auditors' Contract*.

As stated in our engagement letter dated July 18, 2005, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the general purpose financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute, assurance and because we did not perform a detailed examination of all transactions, there is a risk that material errors, fraud or illegal acts may exist and not be detected by us.

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our audit procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the District's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget Circular A-133 Compliance Supplement applicable to each of its major federal programs for the purpose of expressing an opinion on the District's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the District's compliance with those requirements.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the District are described in Note A to the financial statements. There were no changes in significant accounting policies during the year. We noted no transactions entered into by the District during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most significant accounting estimate is the estimate for sick leave.

Significant Audit Adjustments

For purposes of this letter, professional standards define a significant audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the District's financial reporting process (that is, cause future financial statements to be materially misstated). The audit adjustments, in our judgment, do not indicate matters that could have a significant effect on the District's financial reporting process. In addition, management has made all adjustments proposed by us.

Disagreements With Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. There have been no disagreements during the course of our audit.

Consultations With Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters. If a consultation involves application of an accounting principle to the

District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to contact us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditor. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

This report is intended solely for the use of the members of the Board of Education, Kentucky State Committee for School District Audits and management and is not intended and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Shles, Carter & Associates".

Certified Public Accountants
September 23, 2005